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In the

Supreme Court of the United States

OCTOBER TERM, 1967

No. 279

TURNBULL, INC., TRANSFEREE,
Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

On Petition For A Writ of Certiorari To The United States Court of Appeals For The Fifth Circuit

PETITIONER'S REPLY BRIEF

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ASSIGNMENT OF INCOME

Respondent states our position to be "that the rule of *Horst* and *Eubank* applies only when the assignee is 'the natural object of the donor's bounty' and never to be a transaction between 'strangers'." (Memo. p. 3) This over-simplified version would be quite accurate if Respondent had substituted the word "sale" for "transaction".

This is so because the "rule of *Horst*" is premised upon the *satisfaction* of an assignor's economic interests and be-

cause common experience tells us that the only *satisfaction* which one may expect to realize from a transfer to a stranger is the sale price received. The stranger's enjoyment of his profit does not, in common experience, result in vicarious *satisfaction* to the seller, either financially or emotionally. Our reliance on pragmatism is not inappropriate in applying the *Horst* rule.

> "Common understanding and experience are the touchstones for the interpretation of the revenue laws." *Helvering v. Horst*, 311 U.S. 112, 118 (1940)

In *Helvering v. Horst, supra*, this Court ruled that a taxpayer may realize income by the "use or disposition of his power to receive or control the income (so) as to procure in its place *other satisfactions which are of economic worth.*" (311 U.S. 116) (emphasis supplied).

> "Underlying the reasoning in these cases is the thought that income is 'realized' by the assignor because he, who owns or controls the source of income, also controls the disposition of that which he could have received himself and diverts the payment from himself to others *as the means of procuring the satisfaction of his wants.*" (311 U.S. 116-117) (emphasis supplied).
>
> "Even though he never receives the money, he derives money's worth from the disposition of the coupons which he has used as money or money's worth *in the procuring of a satisfaction* which is procurable only by the expenditure of money or money's worth." (311 U.S. 117) (emphasis supplied).

If we could conceive of a pure and altruistic gift of future income rights to a stranger, such an assignment would create no present or future income to the donor because he would not thereby procure the *satisfaction* upon which the

decision in *Horst* relies. It follows, *ipso facto*, that a *sale* for monetary consideration to a stranger creates and simultaneously limits the total *satisfaction* realized by the seller; that *satisfaction* is the amount or value of the price received. This price represents the total realized income "when he who is entitled to receive (future income) makes use of his power to dispose of it *in procuring satisfaction* which he would otherwise procure only by the use of the money when received." (311 U.S. 119) (emphasis supplied).

That this limitation must be applied to a sale to a stranger is conclusively demonstrated by this Court's decision in *Commissioner v. P. G. Lake, Inc.*, 356 U.S. 260 (1958) which actually involved a sale to a non-stranger. Notwithstanding that relationship, the assignor's *satisfaction* was limited to the price he received. Respondent's attempt (Memo. p. 3-4) to limit this case and the many others like it to the issue of capital gains rather than the amount and time of income realization is based on a misconception of the effect of "legal issues". Each of these cases determined the tax consequences of an assignment of income rights for valuable consideration. That is the question here. The holdings of these cases determined time and amount of income. That is the question here. Certainly, Petitioner will not be penalized in securing the application of the *Lake* rule because capital gains were not claimed.

To be sure, as Respondent notes (Memo, p. 3), *the Horst* decision mentioned, by way of example, the possibility that income would be realized if it were assigned for the purpose of securing foodstuffs or satisfying a debt at the "corner

grocery"; this example was combined with that of a charitable contribution or "a gift to his favorite son". However, in the case of the grocery bill, we *know* that the assignor's realized income would be limited to the value of groceries received or the amount of debt actually satisfied. See, e.g., *Watson v. Commissioner*, 345 U.S. 544 (1953).[1]

An assignment of income rights to the grocer would not result in taxation to the assignor of the grocer's subsequent collection of that income; and this result would follow no matter how stale the purchased bread proved to be. The assignor's *satisfaction* results from his ingestion of that bread; the grocer's profit is his alone. In the case at bar, Petitioner's income was limited to the consideration received, even if it later proved to be less valuable than originally contemplated.

Respondent's offhand reference to Petitioner's buyer, Price Construction Co., as an "affiliated corporation" (Memo. p. 4) is completely unjustified and directly refuted by the factual findings below. We have not come so far that the identity of a taxpayer-corporation will be merged into an "affiliation" with another corporation on the ground that they have three shareholders in common, and those holding disproportionate interests. If §482 would not justify the cross-

[1] In *Watson*, the sale of unharvested oranges with an orchard was treated as the sale of future income; but only the $40,000 allocated to the oranges from the sale price was ordinary income to the seller (345 U.S., at 55); he was not taxed on the $126,000 which the buyer later realized on the sale of ripe oranges (*Ernest Watson*, 15 T.C. 800, 806).

See also *Hort v. Commissioner*, 313 U.S. 28 (1949), where the landlord was taxed only on cash received in lieu of future rentals even though the value of the latter exceeded the cash price by $24,494.75.

cutting of these corporate lines, then certainly judicial fiat cannot accomplish it so cavalierly.

In this world of "common understanding and experience", that quality of economic satisfaction which is necessary to the taxation of income received by another can be based only upon a relationship which reflects dependency or, at the least, reciprocal obligation. When the assignment results from a sale to a tax-stranger, the seller's *satisfaction* must be limited to the price received.

TRANSFEREE ISSUE

Petitioner was held below to be liable as a "transferee at law" under a standard deemed to be set by federal cases. Petitioner was held to be estopped to a claim otherwise. These holdings are erroneous and far-reaching in their consequences. They unreasonably expand the statutory procedure available to the Commissioner of Internal Revenue in utilizing what was intended only to be a summary procedure for enforcement of rights that arise under state and not federal law.

Section 6901, Internal Revenue Code, 1954, and its predecessors were designed to give procedural aid to the Commissioner; not to diminish a taxpayer's right to rely on State law as the measure of his secondary liability. The Petitioner here was not charged with liability as a taxpayer, but rather only as a party liable for the debts of another. This Court has ruled that state law establishes the substantive right of the Federal Government to collect taxes from those who

may be secondarily liable. *Commissioner v. Stern*, 357 U.S. 39 (1958). The federal procedure established in the Internal Revenue Code may not be so expanded as to justify the creation of a separate and distinct "transferee liability" which is not founded upon local law for its substance.

For these reasons, the Petition for writ of certiorari should be granted.

Respectfully Submitted,

WENTWORTH T. DURANT

RONALD M. MANKOFF

September 8, 1967

CERTIFICATE OF SERVICE

The undersigned certifies that service of this Petition has been made on counsel for Respondent and the Solicitor General by deposit in the United States Mail, duly addressed with proper air mail postage attached.

WENTWORTH T. DURANT

September 8, 1967